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Entity status issues in the UK law of business organisations and related entities: recurrent uncertainty

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Legislation: Protection from Harassment Act 1997 s.2

Cases: DHN Food Distributors v Tower Hamlets LBC [1976] 1 W.L.R. 852 (CA (Civ Div))

DPP v Dziurzynski [2002] EWHC 1380 (Admin); (2002) 166 J.P. 545 (DC)

R. v St Regis Paper Co Ltd [2011] EWCA Crim 2527; [2012] P.T.S.R. 871 (CA (Crim Div))

R. v W Stevenson & Sons (A Partnership) [2008] EWCA Crim 273; [2008] Bus. L.R. 1200 (CA (Crim Div))

Safeway Stores Ltd v Twigger [2010] EWCA Civ 1472; [2011] 2 All E.R. 841 (CA (Civ Div))

Salomon v Salomon & Co Ltd [1897] A.C. 22 (HL)

Co. L.N. 1 The English law of persons offers up a neat distinction between natural persons and artificial (or legal) persons. Our focus of attention in this review will naturally be directed towards the latter genre. But, in reviewing this category, we will find that in practice the apparent distinctions between natural and artificial persons are not always so clear cut.

THE COMPANY AS A SEPARATE LEGAL ENTITY

This foundational principle was finally laid in stone in English law by the landmark House of Lords precedent of *Salomon v A Salomon & Co Ltd* [1897] A.C. 22. The courts have been left to apply or (more infrequently) disapply this principle in individual cases in a wide range of circumstances ever since then. The main difficulty for practitioners in this regard is the lack of predictability of judicial outcomes. What is fairly predictable however is that the courts will not be supportive of an approach by incorporators that suggests a cherry-picking stance towards adherence to the logical consequences of separate corporate ***Co. L.N. 2*** personality. On this, see the comments of Gross J. at [60] in *Antonio Gramsci Shipping Corp v Recoletos Ltd* [2010] EWHC 1134 (Comm).

The *Salomon* principle is also recognised in legislation. Indeed, it has assumed the status of a legal presumption, to be excluded only in the most explicit of terms. In attempting to understand the statutory life of *Salomon* (above), the starting point must be the Interpretation Act 1978, which by a combination of s.5 and Sch.1 classifies a company as a "person" for the purposes of legislation in general, unless the contrary is intended. This formulation naturally leaves open the possibility for dispute. Thus, new issues continue to be explored by the English courts in this interpretative context.

These questions of interpretation have been at their most acute with regard to the offence created under s.2 of the Protection from Harassment Act 1997. The first issue to determine is whether a company can be harassed for the purposes of this particular legislation: in other words can it be a victim of this crime? In *DPP v Dziurzynski* [2002] EWHC 1380 (Admin); (2002) 166 J.P. 545 the Divisional Court answered this question in the negative insofar as this criminal offence is concerned. For confirmation of this point, note in particular the observations of Rose L.J. at [32]. That said, there are arguments that in civil law an injunction may be appropriate to stop similar behaviour against a company--for this possibility see *Huntingdon Life Sciences Ltd v Curtin* [1997] EWCA Civ 2846. It is also true that the criminal offence in question can be committed against directors and employees of a company thereby creating indirect protection in criminal law for the company itself.

Nevertheless, the ruling of the Divisional Court reflects the artificial construct of a company and marks it out as somewhat different from natural persons. The ruling of the Divisional Court is also consistent with other precedents that seek to deny human characteristics to companies. For comparable precedents see, for example, *Firstcross Ltd v East West (Export/Import) Ltd* (1981) 41 P. & C.R. 145 (inability of a company personally to reside in premises); *R. v Home Secretary, Ex p. Atlantic Commercial Ltd* [1997] B.C.C. 692 (a company cannot be a victim of a miscarriage of justice); *Collins Stewart Ltd v The Financial Times Ltd* [2005] EWHC 262 (QB); [2006] E.M.L.R. 5 (per Gray J. at [31]) (a company cannot experience hurt feelings for the purposes of aggravated damages if libelled). Contrast these restrictive perspectives on the characteristics and attributes of a company with the attitude adopted in *R. v Broadcasting Standards Commission Ex p. BBC* [2001] Q.B. 885; [2001] B.C.C. 432, where the Court of Appeal indicated that a company was capable of enjoying a right of privacy. We have also intimated above that it is well established that a company can sue for defamation, as was indicated in *South Hetton Coal Co Ltd v North Eastern News Association Ltd* [1894] 1 Q.B. 133. One suspects that the outcomes here are driven more by judicial attitudes towards the underlying policy of the legislation under review and less by a desire to adopt a consistent approach towards the essential ingredients of corporate personality. From a corporate lawyer's perspective, that is regrettable and simply lays the grounds for further litigation.

Looking at the converse scenario under the 1997 Act, can a company harass a victim for the purposes of the offence under s.2? This issue fell to be considered by Silber J. in *Kosar v Bank of Scotland Plc T/A Halifax* [2011] EWHC 1050 (Admin); [2011] B.C.C. 500. Here the court held that in principle a company was capable of committing harassment. Again an air of inconsistency emerges, but in this case the illogicality is internal to the 1997 Act regime itself.

THE LITIGATING COMPANY

We have noted above a number of issues related to litigation involving companies. But, to recap: a company can be both a claimant and defendant in its own right. It can be awarded damages and have damages awarded against it (even if the claimant is a shareholder--see Companies Act 2006 s.655). Companies can, by virtue of the Civil Procedure Rules r.39.6, now appear in court in England and Wales through an authorised officer, provided the court gives its permission--counsel is not required and the common law rule to that effect (as applied by the Supreme Court in Ireland in *Battle v Irish Art Promotion Centre Ltd* [1968] I.R. 252) is abrogated. (Such representation is not allowed in Scotland: see *Secretary of State for Business, Enterprise and Regulatory Reform v UK Bankruptcy Ltd* [2010] CSIH 80; [2011] B.C.C. 568.) On the exercise of this newly available judicial discretion with regard to allowing corporate representation in the absence of counsel, see the illuminating discussion in *Watson v Bluemoor Properties Ltd* [2002] EWCA Civ 1875; [2003] B.C.C. 382. However, public legal aid (community legal service) is not available to assist a company in litigation: see Access to Justice Act 1999 s.4 and *R. v Chester and North Wales Area Legal Aid Office (No.12), Ex p. Floods of Queensferry Ltd* [1998] B.C.C. 605. Security for costs may be awarded against a litigating company in the same way that security for costs may be awarded against any claimant. The customised rules on security for costs for corporate claimants formerly found in the Companies Act 1985 (see for example s.726) have not been re-enacted in the Companies Act 2006 and the general principles on security for costs, as contained in the Civil Procedure Rules (see rr.25.12 and 25.13), now apply.

ATTRIBUTION ISSUES

A related question concerns the issue as to whether human motivations can be attributed to corporate entities. This has always generated controversy and has required some guidance from eminent jurists. So in *Lennard's Carrying Co Ltd v Asiatic Petroleum Co Ltd* [1915] A.C. 705 Viscount Haldane felt that corporate motivations could be determined by reference to the “directing mind” of the company. This was a narrow formulation. At the

other end of the spectrum, it is clear ***Co. L.N. 3*** that a company should not have the mental state of a junior employee attributed to it: *Tesco Supermarkets Ltd v Nattrass* [1972] A.C. 153. Where to draw the line? The leading modern authority on this conundrum on setting the parameters of attribution liability is the Privy Council decision in *Meridian Global Funds Management Asia Ltd v Securities Commission* [1995] 2 A.C. 500; [1995] B.C.C. 942. Here Lord Hoffmann adopted a wider and more flexible perspective: the critical issue was who, under the constitution of the company, had the authority to perform the act in question. Attribution can, depending on the particular circumstances of the case, apply to the acts of employees who cannot be classed as part of the directing mind of the company in general.

The debate continues. We should now note *Stone & Rolls Ltd v Moore Stephens* [2009] UKHL 39; [2009] 1 A.C. 1391. The House of Lords in this instance concluded by a narrow three to two majority (Lord Phillips, Lord Walker and Lord Brown; with Lord Scott and Lord Mance dissenting) that the maxim ex turpi causa non oritur actio could be applied to prevent a company from suing its auditors for their failure to detect fraud in circumstances where the fraud had been perpetrated by the very person who had formerly controlled the company. He was in effect the company's alter ego and it was therefore disqualified from bringing the claim. This decision would score well on any commonsense rating.

The same disqualifying principle of ex turpi causa was reviewed in a different context in *Safeway Stores Ltd v Twigger* [2010] EWCA Civ 1472; [2011] 1 C.L.C. 80. This is now to be regarded as a key precedent on the issue of corporate and managerial liability under UK competition law. The issue under review was whether, if a company had been fixed with the improper intentions of company officers with the result that it undertook to accept a regulatory sanction, it could then seek an indemnity from them. This possibility, having been accepted in principle at first instance, was decisively rejected by the Court of Appeal. The policy underpinning the Competition Act 1998 was to impose “personal” sanctions on firms--this liability could not then be offloaded onto individuals. The Court of Appeal ruling will come as a relief for company executives but it will do little to encourage appropriate managerial behaviour in this context.

Attribution questions also came to the fore in the curious case of *KR v Royal and Sun Alliance Plc* [2006] EWCA Civ 1454; [2007] B.C.C. 522. The case was concerned with the scope of a care home company's liability insurance cover. The Court of Appeal, again relying on the attribution principles, ruled that the insurance cover was not available to protect against liability for the acts of senior managers of the company but could encompass the actions of more junior employees.

The most recent reported precedent involving the issue of attribution liability is *R. v St Regis Paper Co Ltd* [2011] EWCA Crim 2527. Here it was held by the Court of Appeal that attribution could not apply in the context of a charge relating to the dishonest recording of environmental pollution control (an offence that required mens rea) because the responsible employee in question who had made the false entries was not the directing mind of the company. Although a company might be convicted of a strict liability offence as the result of the actions of an employee who was not the directing mind of the company it would be inappropriate to convict the company in circumstances where proof of dishonesty was required.

Having reviewed this line of cases it must be apparent that there is still uncertainty on where to draw the line. It is no surprise therefore that we should note the existence of a Law Commission Consultation, *Criminal Liability in Regulatory Contexts,* which was launched in 2010. Attribution liability is one of the foci of discussion. This consultation was the subject of a detailed editorial in (2010) 282 Co. L.N. 1 and requires no further comment. We simply await developments.

GROUP CONCERNS

As far as companies are concerned, we move to a different dimension when we are confronted with personality issues in the context of a group of companies. Corporate

groups were not on the radar in the UK when the *Salomon* (above) principle was determined. Orthodoxy now tells us that each company in a group is a separate person, and there is no such thing as a collective group identity. Lord Denning begged to differ from this traditional legal analysis in *DHN Food Distributors Ltd v Tower Hamlets LBC* [1976] 1 W.L.R. 852. The idea of a group as a "single economic entity" was thus born. At the time, this radical approach was treated with universal scorn in the courts across the common law spectrum. But as the decades have passed it appears to be gaining adherents. So in *Beckett Investment Management Group Ltd v Hall* [2007] EWCA Civ 613 at paras [18]-[19] Maurice Kay L.J. used language that was strikingly similar to that of Lord Denning. The decision of Wyn Williams J. in *Chandler v Cape Plc* [2011] EWHC 951 (QB), which was analysed in detail by Professor Griffin in (2011) 300 Co. L.N. 1, in effect also supports this more realistic interpretation of the group. It follows from this ruling that in appropriate circumstances a parent company may therefore owe a duty of care to employees of one of its subsidiaries.

That said, there are still strong voices in favour of the orthodox interpretation of personality distinctions within groups: see for example *Millam v The Print Factory (London) 1991 Ltd* [2007] EWCA Civ 322; [2008] B.C.C. 169 (mere control by parent of a subsidiary company does not of itself justify lifting the veil). Indeed, in *Linsen International Ltd v Humpuss Sea Transport Pte Ltd* [2011] EWHC 2339 (Comm) Flaux J. at [19], [39], [58] and [126] repeatedly rejected the single economic entity approach by indicating that the close association between companies within a group without more does not justify lifting the veil. During the course of his judgment Flaux J. sought to analyse the principles governing the lifting of the veil of separate ***Co. L.N. 4** corporate personality in a group context where there has been an alleged abuse of the corporate structure. In so doing, he drew support from the approach adopted by Munby J. in *Ben Hashem v Ali Shayif* [2008] EWHC 2380 (Fam). Basically it is necessary to establish both the existence of control and the presence of wrongdoing as preconditions to lifting the veil--see [19] (in *Linsen*) again. Control, as such, does not on its own justify disregarding separate personality within a group. Moreover, Flaux J. at [123] and [142] lent his voice in support of the criticisms that have been raised against *Creasey v Breachwood Motors Ltd* [1992] B.C.C. 638, where arguably it was suggested that, through a veil-lifting process, companies within a group could be subject to liabilities which they had not contracted for.

Looking at these authorities in the round the theme of unpredictability looms large when we look at veil lifting, whether in the context of groups or more generally. There is a real need for guidance from the Supreme Court on what is a fundamental feature of our system of corporate law.

Groups consist of holding companies and subsidiaries. How are the latter to be defined? The Companies Act 2006 offers some guidance in the form of s.1159, but the courts have still been called on to offer a more detailed and refined analysis. So in *Enviroco Ltd v Farstad Supply A/S* [2011] UKSC 16; [2011] B.C.C. 511 we were concerned with the meaning of the term subsidiary when used in commercial documentation. The Supreme Court, confirming the view taken in the Court of Appeal, held that before one company (B) could be seen to be a subsidiary of another company (A), it would be required that A was a "member" of B. This is logical.

THE PARTNERSHIP AS ENTITY

History tells us that a partnership under English law is an unincorporated association and therefore is not to be treated as a separate entity. This is true both of the general partnership and the 1907 variant of the limited partnership--see the comments of Farwell J. in *Re Barnard* [1932] Ch. 269. In spite of a recent recommendation from the Law Commissions, *Partnership Law* (2003) (Law Com 283/Scottish Law Com 192) (Cm 6105) that entity status be awarded to the ordinary partnership, the traditional legal position is what we have to work with. That formal stance, however, needs to be contrasted with the provisions of the Interpretation Act 1978 (s.5 and Sch.1) which includes a body of persons unincorporate under the banner of a "person". This lack of clarity on the issue of personality

can cause difficulties in particular circumstances where a statutory provision has to be applied, as was apparent in *R. v W Stevenson & Sons* [2008] EWCA Crim 273; [2008] 2 Cr. App. R. 14. Here the court felt the need to clarify the point that in principle whether a partnership firm had committed an offence or not did not mean that the same offence was also committed by the individual partners. (Although in Scotland under the Partnership Act 1890 s.4(2) a firm is a legal person distinct from the partners of whom it is composed, but an individual partner may be charged on a decree or diligence directed against the firm.)

Similar issues have arisen with regard to issue of liability under the Corporate Manslaughter and Homicide Act 2007. The Act clearly applies to companies and it is specifically applied to partnerships by s.14. Presumably it applies to LLPs because of their corporate status (see s.25 of the 2007 Act).

LIMITED LIABILITY PARTNERSHIPS

Section 1(2) of the Limited Liability Partnerships Act 2000 tells us that an LLP is a corporate entity. So, consequently, it has in effect the unlimited capacity of a natural person (s.1(3)). The government was quite insistent on this perception of the LLP and fiercely resisted the suggestion that the LLP might be construed as a partnership with limited liability. The exceptionally lengthy judgment of Sales J. in *F & C Alternative Investments (Holdings) Ltd v Barthelemy* [2011] EWHC 1731 (Ch) supports this official perspective and shows that the LLP is to be viewed as more like a company than a partnership. Therefore, the fiduciary duties, which one expects to exist between partners inter se, are not applicable to the domestic interactions between LLP members. For further comment on this important case see D. Milman (2011) 303 Co. L.N. 1.

CHARITIES AND UNINCORPORATED ASSOCIATIONS

Although charities are by definition not business organisations, there is no doubting their commercial significance in modern society. They are major employers and suppliers of goods. Charities may take many forms. They may be incorporated (typically as companies limited by guarantee), in which case they are governed by a combination of the Companies Act 2006 (see in particular s.5), the Charities Act 1993 (especially ss.63-69) and the Charities Act 2006 (see ss.28-30). For the former regulatory matrix note for instance that s.42 of the 2006 Act excludes charitable companies from the new relaxed rules on ultra vires contracts. Community interest companies operating a social enterprise (see s.6 of the Companies Act 2006) are another option to consider. Here the Companies (Audit, Investigations and Community Enterprise) Act 2004 still has a role to play in spite of the 2006 consolidation. Finally, it should be mentioned that Ch.8 of the Charities Act 2006 (s.34 and Sch.7) makes available a new model, the “charitable incorporated organisation”, which enjoys corporate personality but does not have to be a registered as a company. All of the above possibilities present no difficulties with regard to the question of entity status.

However, many charities, especially those of more modest ambitions, are not incorporated. Setting aside the special rules for distributing the assets of a defunct charity, with regard to unincorporated associations in general it is worth noting ***Co. L.N. 5*** that an unincorporated club cannot be wound up under the provisions of the Insolvency Act 1986: *Re Witney Town Football and Social Club* [1994] 2 B.C.L.C. 487. The same would appear to be the case with regard to an unincorporated charity: *Gilbert Deya Ministries v Kashmir Broadcasting Corp Ltd* [2010] EWHC 3015 (Ch). Similarly, in *Panter v Rowellian Football Social Club* [2011] EWHC 1301 (Ch), [2011] 2 B.C.L.C. 610 H.H. Judge Behrens ruled that it was not possible to exploit the Insolvency Act 1986 Sch.B1 administration procedures in respect of such a body. Such a club was not a “company” within the meaning of para.111(1A) of Sch.B1 nor was it an “association” for the purposes of s.220(1) of the Act (unregistered companies). Thus, the court dismissed an application by a creditor for an administration order on the grounds of lack of jurisdiction.

Another potential consequence of operating an organisation as an unincorporated

association is that on the membership falling below two the assets prima facie vest in the surviving member--for discussion of the operative principles see the judgment of Lewison J. in *Hanchett-Stamford v Attorney General* [2008] EWHC 330 (Ch), [2009] Ch.173.

Co. L.N. 2011, 306, 1-5

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